

ORIGINAL



0000136631

BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

RECEIVED

DOCKETED

**COMMISSIONERS**

GARY PIERCE - CHAIRMAN

BOB STUMP

SANDRA D. KENNEDY

PAUL NEWMAN

BRENDA BURNS

2012 JUL -6 P 3:54

JUL -6 2012

ARIZONA CORPORATION COMMISSION  
DOCKET CONTROL

DOCKETED BY

M-7

IN THE MATTER OF THE APPLICATION OF  
TUCSON ELECTRIC POWER COMPANY FOR  
APPROVAL OF ITS 2011-2012 ENERGY  
EFFICIENCY IMPLEMENTATION PLAN.

DOCKET NO. E-01933A-11-0055

**TUCSON ELECTRIC POWER COMPANY'S  
LEGAL BRIEF ON THE PROPOSED INTERIM PERFORMANCE INCENTIVE**

Pursuant to the May 16, 2012 Procedural Order in this docket, Tucson Electric Power Company ("TEP" or the "Company"), through undersigned counsel, hereby submits its pre-hearing legal brief regarding the proposed Interim Performance Incentive ("IPI") in TEP's Updated Implementation Plan ("Updated Plan") submitted May 3, 2012. TEP submits that under the Electric Energy Efficiency Rules, A.A.C. R14-2-2401, *et seq.* ("EE Rules"), the Commission can approve the new IPI as part of TEP's Updated Plan and there is no legal requirement to defer that approval to a rate case.<sup>1</sup>

**Background.**

TEP's current performance incentive was approved in TEP's last rate case, in Decision No. 70628 (December 1, 2008) – prior to the adoption of the EE Rules. The existing performance incentive is designed to encourage greater spending by TEP on demand-side management and

<sup>1</sup> Staff's Direct Testimony (at page 14, lines 9-10) states that it believes that an "LFCR be dealt with as part of TEP's upcoming rate case, where it can be fully considered." Although TEP proposed a form of LFCR as part of its 2011-2012 Implementation Plan, it has not proposed an LFCR mechanism in the Updated Plan. The Updated Plan is a carefully negotiated compromise that the Company is willing to accept in lieu of an LFCR which TEP believes it would otherwise be entitled given the confiscatory impacts of the EE Rules on the Company in light of its rate freeze. Although the Company believes that there is no legal impediment to the Commission approving a form of LFCR as part of an EE implementation plan (see TEP's Exceptions to Staff's Proposed Order (filed December 2, 2011)), the issue raised by Staff in its testimony is moot.

1 energy efficiency ("DSM/EE") programs. The current performance incentive is structured to allow  
2 TEP to collect 10% of the net benefits from the DSM portfolio, excluding the Lower Income  
3 Weatherization ("LIW"), Education and Outreach ("E&O") and Direct Load Control Programs,  
4 but is capped at 10% of DSM spending with no variation in the amount of incentive based on  
5 TEP's meeting or exceeding EE Standards. TEP believes this structure provides the wrong signal  
6 for performance incentives, particularly given the new requirements in the EE Rules.

7 In its Updated Plan, TEP proposes a new, IPI that incents cost-effective DSM/EE programs  
8 and actual performance. Specifically, the interim "Energy Efficiency Share Benefits" will include:  
9 (1) a base amount calculated as 7.0% of net benefits and (2) an additional amount based on key  
10 metrics and as detailed in Table 3 of its Updated Plan submitted on May 2, 2012. This structure is  
11 preferable over the percent spending cap because it encourages cost savings rather than increased  
12 spending to increase the performance incentive. It is still a model that places more emphasis on  
13 programs with the best cost-effectiveness and the highest net-benefits. The IPI is a critical  
14 component of the Updated Plan and is supported by RUCO, SWEEP and AECC. But for the IPI,  
15 TEP would not be able to support the Updated Plan which is, in essence, a compromise or  
16 settlement proposal that TEP is willing to live with to bridge the short gap between now and the  
17 conclusion of TEP's pending rate case in Docket No. E-01933A-12-0291 in 2013.

#### 18 **Argument.**

19 The express language of the EE Rules and sound public policy support the approval of  
20 TEP's proposed IPI as part of TEP's Update Plan. The adoption of the new performance  
21 incentive does not have to be done in a rate case proceeding. Moreover, TEP is not seeking the  
22 establishment of an adjustor related to the proposed IPI. The Commission has already approved  
23 a Demand-Side Management Surcharge ("DSMS") for TEP in Decision No. 70628 and has  
24 subsequently approved changes to the amount of the DSMS based on new programs and budgets.  
25 The existing DSMS provides for recover of the existing performance incentive and would be  
26 used to recover the IPI.

1 Staff has argued that a new or modified performance incentive for TEP can only be adopted  
2 in a rate case. See Staff Report, dated November 16, 2011, at pages 47-48.<sup>2</sup> However, as set forth  
3 below, the EE Rules provide that the Commission can set a performance incentive in connection  
4 with the adoption of an EE implementation plan. Moreover, sound public policy supports the  
5 ability to adopt a performance incentive that is related to an implementation plan *at the time* the  
6 implementation plan is adopted.

7 **A. The EE Rules Expressly Provide for Establishing a Performance Incentive in**  
8 **the Implementation Plan Process.**

9 The plain language in A.A.C. R14-2-2411 expressly provides that the Commission can  
10 consider a performance incentive in the implementation process to encourage and reward a utility  
11 for achieving the energy efficiency standard:

12 “In the implementation plans required by R14-2-2405, an affected utility may  
13 propose for Commission review a performance incentive to assist in achieving the  
14 energy efficiency standard set forth in R14-2-2404. The Commission may also  
consider performance incentives in a general rate case.”<sup>3</sup>

15 The EE Rules unequivocally state that it is appropriate for the Commission to review the  
16 performance incentive when requested by an affected utility. That is what TEP is requesting here.  
17 Although the EE Rules acknowledge that performance incentives “*may also*” be addressed in a rate  
18 case, the EE Rules do not *require* it as posited by Staff. Further, the IPI is merely a bridge that is  
19 subject to true-up by the Commission in TEP’s rate case, which will most likely be concluded  
20 within the next 12 months.

21  
22  
23  
24  
25 <sup>2</sup> It should be noted that on page 8, line 21 through page 9, line 2 of Staff’s Direct Testimony filed on June  
26 15, 2012, Staff indicated “*it would be preferable* to review the Performance Incentive mechanism in TEP’s  
27 rate case, where it can be more fully considered, and considered in conjunction with related issues.”  
(Emphasis added.) Based on this statement, it is unclear if Staff is changing its legal position on this issue.

<sup>3</sup> Emphasis added.

1           **B.     The Rulemaking Record Supports Establishing or Modifying a Performance**  
2           **Incentive in Connection with the EE Implementation Plan Process.**

3           A review of the rulemaking process, and particularly the evolution of Rule 2411, reveals  
4           that Rule 2411 was intended to provide for ongoing review and, potentially, revision to a utility's  
5           performance incentive. The initial draft of the EE Rules (issued on October 30, 2009), set forth a  
6           specific structure for performance incentives:<sup>4</sup>

- 7           A.     An affected utility that achieves 85% compliance with the annual energy  
8                   efficiency standard in a calendar year, calculated as provided in subsection  
9                   (B) may recover in the following calendar year, through its Commission-  
              approved cost recovery mechanism, a performance incentive established as  
              provided in the table below:

10

Level of Compliance with Annual Energy Efficiency Standard Achieved (Excluding Net Benefits from Demand Response)	Performance Incentive as a Percentage of Net Benefits from Energy Efficiency Programs	Performance Incentive Capped at a Percentage of Program Costs
85% to 95%	6%	12%
96% to 105%	7%	14%
106% to 115%	8%	16%
116% to 125%	9%	18%
Above 125%	10%	20%

11  
12  
13  
14  
15

- 16           B.     An affected utility shall not include net benefits derived from demand-response  
17                   programs when calculating compliance with the annual energy efficiency standard  
              for purposes of determining the performance incentive under this Section.

18           Several stakeholders, however, expressed concerns with having a specific performance  
19           incentive standard set forth in the EE Rules. Those stakeholders indicated their preference to  
20           have such incentives considered in connection with the implementation plans, so that the  
21           incentives are tied to the objectives of a specific program portfolio and take into account changed  
22           circumstances over time without having to go through another rulemaking process.<sup>5</sup> In response  
23           to these concerns, the Commission amended A.A.C. R14-2-2411 to simply state that: "In the  
24           implementation plans required by R14-2-2405, an affected utility may propose for Commission  
25

26           <sup>4</sup> See proposed A.A.C. R14-2-2411 in Staff's October 30, 2009 Memorandum (Docket No. RE-00000C-09-  
0427).

27           <sup>5</sup> See Comments of Southwestern Energy Efficiency Project ("SWEEP"), Letter from National Resources  
Defense Council, and Letter from Sierra Club in Docket No. RE-00000C-09-0427 (December 11, 2009).

1 review a performance incentive to assist in achieving the energy efficiency standard set forth in  
2 R14-2-2404. The Commission may also consider performance incentives in a general rate case.”  
3 The intent of the new language was to determine the structure of performance incentives  
4 primarily during the evaluation of implementation plans, although it left open the option to  
5 determine such a structure in a rate case. This new language was approved in Decision No.  
6 71436 (December 18, 2009) which opened the rulemaking docket for the EE Rules. The final  
7 EEE Rules were approved in Decision No. 71819 (August 10, 2010) with the amended  
8 performance incentive language intact.

9 **C. The Commission Has Recently Confirmed Its Intent to Review Performance**  
10 **Incentives in Connection with EE Implementation Plans.**

11 In the recent Arizona Public Service Company (“APS”) rate case, the Commission  
12 reinforced its intention to establish or modify a performance incentive on an annual basis during  
13 the implementation plan even if the performance incentive is adopted in a rate case. In Decision  
14 No. 73183 (May 24, 2012), the Commission reaffirmed that performance incentives are part and  
15 parcel with the implementation plans; and there should be flexibility to determine the structure of  
16 those incentives within the process of evaluating those plans:

17 “While we appreciate the ability and opportunity to develop new performance  
18 incentives tied to energy efficiency, we believe that Performance Incentives, just  
19 like the implementation plan that they are parcel of, should be reviewed and  
20 established on an annual or periodic basis as part of the [Demand-Side  
21 Management Adjustment Clause]. As conditions change for each implementation  
22 plan, there should be flexibility in how performance incentives are structured,  
23 including the flexibility to eliminate Performance Incentives for any given year.  
24 Therefore, performance incentive formulas will be deliberated and determined in  
25 each implementation plan.”<sup>6</sup>

26 This provision, initially proposed in an amendment by Commissioner Burns, further  
27 clarifies that the Commission does not want to limit its review of performance incentives adopted  
in a rate case only in the next rate case. This approach reflects sound policy for timely review

---

<sup>6</sup> Decision No. 73183 at 41.

1 and modification that can address the current circumstances without binding the Commission to  
2 a delayed or cumbersome process for review and modification. Rule 2411 embodies this sound  
3 approach and certainly can be interpreted to meet the Commission's view of the appropriate time  
4 to review and modify performance incentives.

5 **Conclusion.**

6 Under the plain language - and the intent - of A.A.C. R14-2-2411, as well as the recent  
7 Commission confirmation provided in Decision No. 73183, the Commission has the legal  
8 authority to adopt TEP's proposed IPI as part of the Updated Plan.

9 RESPECTFULLY SUBMITTED this 6<sup>th</sup> day of July 2012.

10 Tucson Electric Power Company

11  
12  
13 By



14 Michael W. Patten  
15 Jason D. Gellman  
16 Roshka DeWulf and Patten  
17 One Arizona Center  
400 East Van Buren Street, Suite 800  
Phoenix, Arizona 85004

18 and

19 Bradley S. Carroll  
20 Tucson Electric Power Company  
21 88 East Broadway, MS HQE910  
22 P.O. Box 711  
Tucson, Arizona 85702

23 Attorneys for Tucson Electric Power Company

24 Original and 13 copies of the foregoing  
25 filed this 6<sup>th</sup> day of July 2012, with:

26 Docket Control  
27 Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

1 Copy of the foregoing hand-delivered/e-mailed  
2 this 6<sup>th</sup> day of July 2012 to:

3 Jane Rodda, Administrative Law Judge  
4 Hearing Division  
5 Arizona Corporation Commission  
6 400 West Congress  
7 Tucson, Arizona 85701

8 Charles Hains, Esq.  
9 Scott Hesla, Esq.  
10 Legal Division  
11 Arizona Corporation Commission  
12 1200 West Washington Street  
13 Phoenix, Arizona 85007

14 Steve Olea  
15 Director, Utilities Division  
16 Arizona Corporation Commission  
17 1200 West Washington Street  
18 Phoenix, Arizona 85007

19 C. Webb Crockett  
20 Patrick J. Black  
21 Fennemore Craig, PC  
22 3003 North Central Avenue, Suite 2600  
23 Phoenix, Arizona 85012  
24 Attorneys for Freeport-McMoRan and AECC

25 Timothy Hogan  
26 Arizona Center for Law  
27 in the Public Interest  
202 East McDowell Road, Suite 153  
Phoenix, Arizona 85004

David Berry  
Western Resource Advocates  
P. O. Box `064  
Scottsdale, Arizona 85252

Jeff Schlegel  
SWEEP  
1167 W. Samalayuca Dr.  
Tucson, Arizona 85704

Daniel Pozefsky, Chief Counsel  
Residential Utility Consumer Office  
1100 West Washington, Suite 220  
Phoenix, Arizona 85007

1 Larry Robertson  
2 Of Counsel to Munger Chadwick PLC  
3 P. O. Box 1448  
4 2247 E. Frontage Road  
5 Tubac, Arizona 85646

6 By Mary Appolito  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27